September 29, 2000

DONNA M. PEAK
ACTING VICE PRESIDENT,
FINANCE, CONTROLLER

SUBJECT: Audit Report - Equity Loss Payments
(Report Number FT-AR-00-004)

This report addresses payments for losses on real estate transactions incurred as part of the Postal Service's relocation program. The Board of Governors requested the overall audit on relocation benefits. This is the third in a series of reports[1] examining relocation benefits for Postal Service executives. Our relocation work is continuing and future reports will address other aspects of relocation benefits for Postal Service executives.

Results in Brief

Through benchmarking, we confirmed that the Postal Service policy of reimbursing employees for losses incurred on real estate transactions was similar to policies of the private sector and other government agencies. In addition, we found that payments were calculated properly based on the verbal formulas provided by Postal Service officials. However, controls over equity loss payments needed improvement. We are providing three recommendations to address the issues identified in this report.

Management agreed with two recommendations to fully document policies and procedures for equity loss calculation and reimbursement; and develop and publish a list of approved capital improvements used in determining loss on the sale of an employee's home. However, management disagreed with our recommendation to record miscellaneous expense allowances and equity loss payments in separate accounts. We will not pursue

[1] The first report in this series was published on May 2, 2000, Relocation Benefits for Postal Service Officers (Report Number FR-FA-00-010(R)). The second report was published on September 28, 2000, Miscellaneous Relocation Expense Payments (Report Number FT-AR-00-001).

resolution of this recommendation at this time. Instead, we plan to reexamine this issue in future financial statement audits. Management's comments, in their entirety, are included in the appendix.

Background

The Postal Service provides loss protection on real estate transactions to employees who change official duty station and sell their primary residences at a loss. This benefit is allowed to all executive and administrative schedule employees and above on a progressive scale as shown in Table 1.

Table 1. Reimbursement Scale

Reimbursement %	PCES	EAS
100%	First $50,000	First $25,000
50%	Next $50,000	Next $25,000
25%	Over $100,000	Over $50,000

An employee must provide appropriate documentation to support the loss amounts, such as a copy of the purchase settlement statement and the sales contract. Corporate Accounting is responsible for evaluating and approving equity loss payments. Upon approval, requests for equity loss reimbursements are filed on PS Form 1012, Travel and Expenses Voucher.

Objective, Scope, and Methodology

Our audit objectives were to determine whether equity loss benefits were comparable with private industry and other government agencies and controls over equity loss payments were adequate. In addition, we determined whether payments were calculated in accordance with the formulas.

To accomplish our objectives we:

- Reviewed Postal Service relocation policies and procedures.

- Reviewed payments in excess of $10,000 from the miscellaneous expense account[2] that were made between fiscal year (FY) 1997 to May 2000.[3]

- Reviewed Internal Revenue Service relocation guidelines.

- Interviewed appropriate Postal Service officials.

- Benchmarked with other nonappropriated government agencies (including quasi-government organizations) and Fortune 500 companies.

In conducting our review, we identified 125 miscellaneous expense allowance payments over $10,000. Upon further analysis, we determined that the account was comprised of miscellaneous expense allowance[4] and the equity loss payments. Of the 125 payments we reviewed, 79 were equity loss reimbursements that totaled over $1.7 million.

This audit was conducted from May 2000 through September 2000 in accordance with generally accepted government auditing standards and included such tests of internal controls as were considered necessary under the circumstances. We discussed our conclusions and observations with appropriate management officials and included their comments, where appropriate.

Benchmarking

We determined that the Postal Service's equity loss program was comparable to those offered by the private sector and similar government agencies. Specifically, we surveyed 35 fortune 500 companies and 8 nontaxpayer funded government agencies. We found that of the 29 entities that responded, 24 had equity loss programs, as shown in Table 2. These entities reimbursed employees for equity losses ranging from 5 to 100 percent of the total loss.

[2] General ledger account 51239.
[3] In addition, we identified 62 employees of the Office of Inspector General who have received miscellaneous expense allowances between January 1997 and May 2000. Fifty-four OIG employees received allowances of $2,500, and eight employees received allowances of $10,000.
[4] Miscellaneous expense allowances are payments given to employees who have been authorized a permanent change of station relating to relocation. This payment is initiated to cover costs such as disconnecting and connecting appliances and utilities, cutting and fitting rugs, and registering automobiles.

Table 2. Benchmarking Results

Existing Equity Loss Program	Nontaxpayer Funded Government Agencies	Fortune 500 Organizations
Yes	4	20
No	2	3
No Response	2	12

Controls Over Equity Loss Payments

Control over equity loss payments needed improvement. We noted that the formulas used by the Postal Service to calculate equity loss payments were not documented. In addition, the items considered to be capital improvements and used to calculate the equity loss payments had not been documented. Postal Service personnel insisted that every effort was made to be consistent in administering the equity loss program. However, without documented policies and procedures, the potential for inconsistent determination of equity loss payments is increased.

In addition, we found that equity loss payments were recorded in the same general ledger account as miscellaneous expense allowances. As a result, the Postal Service's ability to monitor the amount of equity loss and miscellaneous expense allowance payments may be hindered.

Formulas

Formulas to calculate equity loss payments were not documented because other projects had a higher priority. We recalculated 79 equity loss payments that were made during the period of FY 1997 through May 2000 using the formulas that were verbally conveyed to us by postal officials. We found only one payment that was inconsistent with the formula that resulted in a $1,800 difference. Postal personnel stated that they made a mistake in calculating this payment.

Listing of Capital Improvements

The Postal Service allows employees to add the cost of certain home improvements to the purchase price of their home when determining equity loss reimbursements. However, the Postal Service did not have a formal definition of what is considered to be a capital improvement. For instance, the Postal Service considers landscaping completed in the first year and portions of other costs (e.g. one-half of the cost of a swimming pool) to be eligible costs for reimbursement under the equity loss reimbursement program. According to Postal Service officials, a list of approved capital improvements was not developed because it would be too long.

Internal Revenue Service Publication 523, “Selling Your Home,” contains a list of capital improvements. As shown in Table 3, the Internal Revenue Service includes items such as additions to homes, certain lawn and grounds improvements, and other items that are not considered routine maintenance to be capital improvements.

Table 3. IRS Capital Items

Additions	**Heating and Air Conditioning**	**Lawn and Grounds**
Bedroom	Heating System	Landscaping
Bathroom	Central Air	Driveway
Deck	Furnace	Walkway
Garage	Duct Work	Fence
Porch	Central Humidifier	Retaining wall
Patio		Sprinkler system
	Miscellaneous	Swimming pool
	New Roof	
Interior Improvements	Storm Windows, Doors	**Plumbing**
Built-in appliances	Central vacuum	Septic system
Kitchen modernization	Wiring upgrades	Water heater
Flooring	Satellite dish	Softwater system
Wall-to-wall carpet	Security system	Filtration system

We believe that the Postal Service could use the Internal Revenue Service definition to provide a consistent definition of items that are considered a capital improvement. Without documented policies and procedures, the potential for inconsistent determination of equity loss payments is increased.

Recording of Equity Loss Payments

Equity loss payments were combined with miscellaneous expense allowances in the same general ledger account. Postal Service personnel stated that a separate account was not created because it was not practical to set up a general ledger account for such an infrequent occurrence.

By combining these two types of expenses in the same account, the Postal Service is unable to readily determine the total amount of equity loss reimbursements. As a result, the Postal Service's ability to monitor the amount of equity loss and miscellaneous expense allowance payments may be hindered.

According to General Accounting Office standards for internal control in the federal government, organizations should have control activities that help to ensure that all transactions and events are completely and accurately recorded. Additionally, operational and financial information should be recorded and communicated to management in a form that enables them to make operating decisions, monitor performance, and allocate resources.

Postal Service officials stated that it was impractical to establish a general ledger account for an item as infrequent as equity losses. However, the Postal Service has a general ledger account that tracks the costs of the shared real estate appreciation loan program. This account tracks the expenses for 26 employees.

A separate account for equity losses would provide the Postal Service with a more accurate assessment of equity loss payments. Such information would facilitate analysis of relocation benefits and enhance the Postal Service's ability to accurately assess the magnitude of equity loss payments and how such expenses affect its fiscal operations.

Recommendation

The chief financial officer should:

1. Fully document policies and procedures for equity loss calculation and reimbursement.

Management's Comments

Management concurred with this recommendation and stated that by early 2001 the vice president, Finance, Controller will update the relocation handbook to include the policies and process to be followed for equity loss calculation and reimbursement.

Evaluation of Management Comments

Management's comments were responsive to our recommendation.

Recommendation	The chief financial officer should: 2. Develop and publish a list of approved capital improvements used in determining loss on the sale of an employee's home.
Management's Comments	Management concurred with this recommendation and will include in the relocation handbook items outlined in their previous policy letters that may be considered in claiming equity loss.
Evaluation of Management Comments	Management's comments were responsive to our recommendation.
Recommendation	The chief financial officer should: 3. Record miscellaneous expense allowances and equity loss payments in separate accounts.
Management's Comments	Management disagreed with this recommendation. Management stated that over the past four years, less than 100 employees received equity loss reimbursements totaling less than $2 million. Management cited the costs of establishing and maintaining general ledger accounts as one reason for not recording miscellaneous expense allowances and equity loss payments in separate accounts. Management is in the process of reducing general ledger accounts that do not have significant volumes to create efficiencies in their accounting systems. Management also stated that since equity loss reimbursements and miscellaneous expense allowances have the same individual tax reporting features, there was no overwhelming reason to change their account structure.
Evaluation of Management Comments	We disagree with management's assertion that that there was no overwhelming reason to record miscellaneous expense allowances and equity loss payments in separate accounts. While management stated that they were in the process of reducing general ledger accounts, we noted an increase of 46 general ledger accounts between September 1998 and September 2000. Twenty-two of these new accounts were established to record expenses. We also

noted that the Postal Service maintains separate general ledger accounts for other relocation expenses, such as advance round trips, en route travel, temporary quarters, and residence purchases and sales, even though each of these relocation benefits has the same individual tax reporting features of equity loss reimbursements and miscellaneous expense allowances.

We still contend that a separate account for equity losses would provide the Postal Service with a more accurate assessment of equity loss payments. Such an account would allow the Postal Service to better assess the magnitude of equity loss payments and how such expenses affect its fiscal operations. However, we will not pursue resolution of this recommendation at this time. Instead, we will reexamine this issue in future financial statement audits.

Additional Management Comments

Management raised an issue in their response regarding communication of audit observations and conclusions with appropriate management officials. We believe the issues were discussed with appropriate management officials during fieldwork. However, prior to final release of this report, we met with the acting vice president, finance, controller, and agreed that formal exit conferences will be scheduled on all future Finance audits.

We will incorporate the results of this audit into our summary report on relocation benefits. We appreciated the cooperation and courtesies provided by your staff during the review. If you have any questions, please contact John Seeba or me at (703) 248-2300.

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Acting Assistant Inspector General
for Business Operations

cc: Mary Anne Gibbons
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APPENDIX. MANAGEMENT'S COMMENTS

FINANCE

UNITED STATES POSTAL SERVICE

September 25, 2000

KARLA CORCORAN

SUBJECT: Audit Report-Equity Loss Payments

This report was referred to me for response, as the vice president, finance, controller has functional responsibility.

Before providing our responses to your specific recommendations, I need to note a few items. You mentioned your benchmarking efforts in this report. As requested in our response to your previous report, please provide your benchmarking data. We would now like to have the data used in both reports. Your report states that you discussed your conclusions and observations with appropriate management officials. The only item that was discussed with my management team was the incorrect addition of one reimbursement request, resulting in an inconsistency of the formula by $1,800. No other item was mentioned. Therefore, in the future we recommend formal exit conferences with written agendas for all reports within the Finance function.

We are pleased that the auditors found consistency in our equity loss program, as evidenced by only the citing of one mathematical error in four years. As we previously noted, relocation in the Postal Service is an integral and a carefully designed part of the entire employee work program and is intended to meet the organization's need for leadership, flexibility, and outstanding customer service. It would be a mistake to consider it as a stand-alone program, out of context. We hire employees, train employees, and offer employees growth through promotional opportunities and other varied experiences during their careers, while expecting our professional executives to deliver for our customers and us. Providing congressionally mandated universal service requires our executives to develop a broad national perspective, and to have varied experiences in different parts of the organization, so that they can competently fill increasingly responsible leadership positions. As with many large companies whose organizations are spread across this country, this means that postal executives are frequently required to move from one location to another. Often such moves require considerable sacrifice on the part of our executives: uprooting their families or commuting longer distances to be with their families; leaving good friends; dealing with higher costs of living; adapting to new environments, schools, and communities. Relocation can be summarized as a stressful time in our employee's career, and our goal is to provide prompt, consistent service.

We see nothing in this report, or management's response, which contains proprietary or other business information that may be exempt from disclosure under the Freedom of Information Act (FOIA).

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Recommendation 1: Fully document policies and procedures for equity loss calculation and reimbursement. As our policy for equity loss was outlined in previous letters and we plan to update our relocation handbook, we concur. We will include the policies and process to be followed. As outlined in our earlier response, we plan to have the Relocation handbook updated in early 2001.

Recommendation 2: Develop and publish a list of approved capital improvements used in determining loss on the sale of an employee's home. We will include in the relocation handbook items outlined in our previous policy letters that may be considered in claiming equity loss. However we do not concur with the comment that we should use the IRS definition of capital improvements. When selling a home, IRS considers many items including painting and replacing fences and roofs that we consider normal maintenance. Additionally, the auditors did not provide a cost of such a proposal.

Recommendation 3: Record miscellaneous expense allowances and equity loss payments in separate accounts. We disagree with the recommendation. The auditors did not provide a reason for the recommendation other than it might be helpful, that is, they did not identify an internal control issue. Over the past four years, less than 100 employees received equity loss reimbursements, and as pointed out in the report, these total less than $2 million. As we are sure the auditors are aware, establishing and maintaining account numbers costs the USPS. We are in the process of reducing account numbers that do not have significant volumes to create efficiencies in our systems. Additionally equity loss reimbursements have the same individual tax reporting features as the miscellaneous allowance. Therefore, we see no overwhelming reason to change the account structure. The auditors point out that we track expenses for the Shared Appreciation Loan program; however, these are not expenses. They are accounts receivable with, again, different tax reporting consequences.

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cc: Richard J. Strasser, Jr.
Mary Anne Gibbons